RECENT SALES AND INCOME TAX HIGHLIGHTS (THE INTERESTING "STUFF")

Arizona Tax Conference

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GPLET and Sales & Use Tax Legislation

GPLET Reform: H.B. 2213, Ch. 120 (2017)

- Reforms the Government Property Lease Excise Tax (GPLET)
- What is GPLET - Background
  - Government owned property is tax exempt
  - GPLET is an excise tax imposed on a lessee of government owned property (city, town, county or county stadium district)
  - Measured by square footage and use of the building rather than property value
    - Example

1 Story Office Building	-	$2.20
7 Story Office Building	-	$2.53
8 and more stories	-	$3.41

  - GPLET replaced the possessory interest tax in 1996
    - PIT was struck down twice by the Tax Court as unconstitutional

GPLET Reform: H.B. 2213, Ch. 120 (2017) (cont.)

- GPLET is an economic development tools for cities
  - Developer builds high rise, conveys it to city and leases it back – AVOIDS PROPERTY TAX
- GPLET lease can be no longer than 25 years
- First 8 years abated if area is a “slum and blight” area or located inside single central business district

GPLET Reform: H.B. 2213, Ch. 120 (2017) (cont.)

- What HB 2213 does
  - Prospective only: does not affect existing deals
  - Limits term of lease to 8 years from 25 if abatement is involved
  - In year 9, the city conveys property back to developer and it goes on property tax rolls
  - If no abatement involved, 25 year lease term still applies

March 2017

ATRA Supports HB2213

Reforms Government Property Lease Excise Tax (GPLET)

- Mechanism to tax private business on certain property tax exempt government properties
- An "excise" tax that is based on the square footage & use of a building rather than property value
- An 8 year abatement (no tax) is allowed in "slum & blight" single, central business districts (CBD)
- Currently $750+ million in abated property value statewide

HOW DOES GPLET WORK NOW?

- If property is not abated, GPLET collections distributed to taxing jurisdictions as follows:
  - Counties-13%
  - Community Colleges-7%
  - Cities & Towns-7%
  - School Districts-73%
- Lessee calculates & remits GPLET tax
- Property may be exempt from GPLET for 8 yrs if
  - Area is "slum & blight" (loosely defined)
  - Located inside single CBD
- Developers demand GPLET; want best deal possible
- Similarly situated businesses on uneven playing fields
- Pre-2010 rates well below actual property taxes

AUDITOR GENERAL SPECIAL AUDIT

- Dec 2015: OAG audit exposes several flaws
  - Hundreds of thousands in uncollected taxes due to errors
  - Errors lead to higher State GF payouts
- GPLET: "Lacks adequate procedures"
  - Lessees responsible for calculation of tax is problematic
  - Gov lessors must ensure correct tax paid
- Grandfathering clause
  - Just 16 leases of 268 identified subject to 2010 rates
  - GPLETs will not provide the revenue the 2010 law projected

Taxpayer GPLET

Examples of GPLET fairness issues

*Property Tax due

"It's rare for the Auditor General to write such a scathing review of an entire program; GPLET absolutely must be reformed. Moreover, we cannot allow one-off tax breaks which completely cut out the K-12 school districts. GPLET creates unfair tax burdens for everyone and my legislation is a step in the right direction." –Rep. Vince Leach

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Tax Authorization: S.B. 1152, Ch. 332 (2017) Voter Approval of New TPT Must be Held at General Election

- Mandates that election for the approval or authorization of the assessment of transaction privilege taxes by a county or municipality must be held on the first Tuesday after the first Monday in November in an even-numbered year (a statewide general election).
  - And not at special elections where no one shows up.
- Effective January 1, 2018.

Tax Corrections: S.B. 1289, Ch. 156 (2016) Gift Cards Not Subject to Use Tax

- Makes numerous technical changes to Arizona's sales tax laws, including:
  - Clarifies that purchases of "cash equivalents" like gift cards, gift certificates, traveler's checks, and money orders are not subject to use tax
    - Clarification for sales tax was made in 2013
    - **Note:** Pre-paid calling cards are subject to sales or use tax at the time of purchase.

Billboards: S.B. 1310, Ch. 223 (2016)
Billboards Are Not Rentals but Non-Taxable Advertising

- Clarifies that sales tax on rentals of tangible personal property under A.R.S. § 42-5071 (rental of personal property classification) Does not apply to the leasing or renting of billboards that are designed, intended, or used for advertising or information
- Billboard must be visible from a street, road, or other highway (e.g., advertising)
- Codifies the result in *Jones Outdoor Advertising, Inc. v. ADOR,* 1-CA-TX 14-0006 (7/16/2015)

New Online Lodging Classification: S.B. 1350, Ch. 208 (2016) (Airbnb & VRBO)

- Effective January 1, 2017, creates the "online lodging" classification, A.R.S. § 42-5076, imposes a 5.5% state tax on operating an online lodging marketplace
  - Tax base is measured by the total amount charged for the online transaction by the lodging operator
  - Only applies if marketplace has entered an agreement to register
  - Clarifies that tax on transient lodging does not apply
  - Municipalities are permitted to impose a tax as well
- An "online lodging marketplace" is a digital platform through which unaffiliated third parties offer to rent accommodations not classified as commercial or industrial (i.e., AirBNB and VRBO.com)
- Tax cannot be collected from operators (e.g., homeowners) who have written documentation from the marketplace that it will remit the tax
- Permits licensed real estate brokers to obtain sales tax licenses and file consolidated sales tax returns for the properties they manage

Direct Shipment of Wine: S.B. 1381, Ch. 76 (2016)

- Arizona wineries permitted to ship limited quantities of wine directly to Arizona consumers annually
  - Until December 31, 2017, up to six nine-liter cases
  - From January 1 through December 31, 2018, up to nine nine-liter cases
  - Beginning January 1, 2019 up to twelve nine-liter cases annually

- Requires a license from the state, which must be renewed annually

- Wineries required to pay luxury privilege taxes under A.R.S. § 42-3355 on shipments directly to consumers

Taxi & Limo Exemption: S.B. 1492, Ch. 171 (2016)

- Adds exemption for owners and drivers of licensed taxis, livery vehicles, and limousines transporting persons for hire to A.R.S. § 42-5063

- Matches sales tax exemption for “transportation network” drivers and companies (i.e., Uber and Lyft) passed in 2015

- Effective September 1, 2016

Agricultural Aircraft: H.B. 2133, Ch. 181 (2016) Crop Dusters Are Exempt From TPT

- Adds an exemption for new agricultural aircraft used in the commercial production of agricultural, horticultural, viticultural, and floricultural products to A.R.S. § § 42-5159 and 42-5161
- “Agricultural aircraft” means aircraft built for the aerial application of pesticides or fertilizer or for aerial seeding
- Retroactive to April 17, 1985; however, significant limitations on refunds apply
  - Claims must be submitted by December 31, 2016
  - Aggregate refunds issues by Department of Revenue will not exceed $10,000

Charter Aircraft Exemption: H.B. 2533, Ch. 367 (2016) Aircraft Exemption Extended to Cover Most All Aircraft for Hire

- Extends the deduction for aircraft, navigational and communications equipment, and other accessories or equipment sold to persons with certain federal certifications to transport persons or property for hire
  - Exemption now covers most aircraft that transport persons or property for hire
- Includes sales of such items to parties that will lease or otherwise transfer operational control of the aircraft or equipment for at least 50% of the aircraft's flight hours
- Effective July 1, 2017
  - Then retroactive to June 1, 1998 with significant limitations on refunds
- Addresses gap in statute identified in *American Helicopters et al. v. ADOR*, 1-CA-TX 14-0001 (1/24/2015) (helicopters used for charter tours of Grand Canyon did not qualify under the old exemption)

Fractional Aircraft Ownership: S.B. 1416, Ch. 30 (2017)

- Clarifies that the aircraft exemption (*see* H.B. 2533, 2016) includes aircraft sold for use in a fractional ownership program for TPT and use tax.
- Effective: August 9, 2017

Fine Art Exemption: H.B. 2536, Ch. 368 (2016)
TPT Exemption for Scottsdale Art Galleries

- Exempts sales of "works of fine art" to nonresidents at an art auction or gallery within Arizona but for use outside the state if the vendor ships the art to an out-of-state destination
- "Works of fine art" includes:
  - A painting, drawing, sculpture, mosaic or photograph;
  - A work of calligraphy;
  - A work of graphic art, including etchings, lithographs, offset print, or silk screen;
  - A craft work in materials including clay, textile, fiber, wood, metal, plastic, or glass;
  - A work in mixed media, including a collage or a work consisting of any combination of the above
- Effective September 1, 2016
- Limited reinstatement of an exemption eliminated during sales tax simplification initiative
  - Prior exemption was not limited to fine art but included all types of tangible personal property
- See A.R.S. § 42-5061(A)(60)

Electricity for Manufacturing: H.B. 2676, Ch. 374 (2016) Exemption Extended to Cover Intel

- Amends the definition of "manufacturing" used to determine whether a business qualifies for an exemption for purchases of electricity and natural gas under A.R.S. § 42-5063(C)(6).
  - "Manufacturing" now includes "processing" and "fabricating," but excludes publishing and packaging
- Eliminates requirement that at least 51% of the electricity must be used in manufacturing or smelting operations
- Requires utility companies claiming the deduction to report the names and addresses of their qualifying customers
- Also applies at the municipal level
- Effective January 1, 2017

Sales & Use Tax Cases & Rulings

Ariz. Electric Power Cooperative, Inc. v. ADOR

1 CA-TX 16-0004 (Mar. 28, 2017)

Coal and natural gas purchased from out-of-state vendors are subject to Arizona's use tax

- Decision: Coal and natural gas purchased for use in electricity generation is not a nontaxable purchase for resale or exempt from use tax as tangible personal property that becomes a component part of a substance or commodity for sale.
  - Arizona Electric Power ("AEPCO") buys coal and natural gas from out-of-state vendors to generate electricity for sale.
  - Based on expert testimony from both parties, the court determined that AEPCO's expert did not adequately explain how AEPCO holds the coal and natural gas for resale. Instead, the court determined that AEPCO uses and consumes the fuel in the process of generating electricity.
  - The court also determined that purchase of the coal and natural gas AEPCO was using to generate electricity was not exempt under A.R.S. § 42-5159(A)(4) because the coal and natural gas were consumed in the electricity generation process and did not "directly enter[] into or become[] an ingredient or component part of" the electricity.
    - The court relied on the Department's use tax regulation, Ariz. Admin. Code R15-5-121, which says, "The sale of fuel used or consumed in a manufacturing process is taxable" and "[t]he fuel is not considered to be incorporated into the manufactured product."

APS v. City of San Luis

1 CA-TX 16-0009 (August 3, 2017)

Taxing authorities must comply with Constitutional due process requirements when providing notice of amendments to tax codes and laws

- Decision: The City violated APS's due process rights when it failed to provide reasonable notice reflecting the repeal of a franchise fee credit.
  - The City adopted Ordinance No. 253 repealing a franchise fee credit paid by utility providers.
    - APS was the only utility provider affected by the ordinance.
  - The City did not send notice of the ordinance to APS, the League of Arizona Cities and Towns, the Municipal Tax Code Commission, or the Department of Revenue.
  - The City also failed to amend the tax code on file with the City Clerk and attach copies of the ordinance to the tax code.
  - The City audited APS and assessed additional tax based on the ordinance.
  - APS challenged the assessment on due process grounds, amongst other challenges.
  - The tax court granted summary judgment for APS on due process grounds.
  - The Court of Appeals affirmed the judgment for APS because the City failed to provide reasonable notice of the ordinance repealing the franchise fee credit to APS by not reflecting the change in any publically available source except town council meeting minutes.

Peters v. City of Prescott

1 CA-TX 15-0004 (Mar. 26, 2016) (not for publication)

Customers do not have standing to challenge sales tax passed through by the business

- Decision: Customers do not have standing to challenge a transaction privilege tax passed through by a business because the customers are not "taxpayers."
  - Prescott imposed a 2% transaction privilege tax on gross income from golf courses, which the courses passed through to their customers
  - A golf course customer challenged the application of the tax to his club dues
  - Prescott City Code allows "taxpayers" to contest an assessment
    - Defines "taxpayer" as "any person liable for any tax"
  - Court of Appeals held that the a "taxpayer" is the party upon whom the legal incidence of a tax is imposed
    - Legal incidence of the tax is on the golf course, even though it is allowed to pass the economic incidence of the tax on to the customer
    - Customer is not a "taxpayer" because the legal incidence of the tax falls elsewhere

Ziegfield Inc. v. ADOR

1 CA-TX 16-0001 (Oct. 6, 2016)

Cabaret shows are taxable under amusement classification

- Decision: Performance at an adult cabaret are "shows" under Arizona's transaction privilege tax amusement classification, and the fees the cabaret collected from the performers and patrons were taxable under Arizona's transaction privilege tax.
  - Taxpayer operated an adult cabaret and requested a refund of transaction privilege taxes
  - Department audited Taxpayer and issued a deficiency under the amusements classification
  - Tax Court granted summary judgment for Department
  - Court of Appeals affirmed the decision because performances at the cabaret constituted a "show of any type or nature" under A.R.S. § 42-5073
    - Court of Appeals also affirmed assessment of transaction privilege tax against door fees, house fees, manager fees, couch fees, and VIP fees that Taxpayer collected because they were all income derived directly or indirectly from the cabaret's shows.

Chevron U.S.A. Inc. v. ADOR

1 CA-TX 16-0001 (Oct. 6, 2016)

Oils and greases are exempt machinery and equipment

- Decision: Oils and greases came within the common understanding of the term "equipment" and were thus exempt from sales tax.
  - Chevron sold oils and greases to Freeport-McMoRan for use in its mining and metallurgical operations
    - The oils and greases reduced friction, dispersed heat, suspended contaminants, and performed other functions enabling the mining equipment to function
  - Court of Appeals found that considering the oils and greases "equipment" is consistent with the Department's position on the exemption of materials like motor oil and antifreeze
    - Sales of those materials to certain lessees of motor vehicles are exempt from taxation because they are part of the vehicle, even though they may require frequent replacement
  - Court also rejected the Department's argument that the oils and greases did not qualify for the exemption because they were "expendable materials"
    - Court held that the Arizona legislature eliminated the "useful life" limitation in 1999 when it amended A.R.S. § 42-5061(C)(1)

Private Taxpayer Ruling LR 16-008

- Ruling: Masticating shrubs on grassland is not taxable contracting
  - The Department likened masticating shrubs on grassland to lawn maintenance services rather than taxable landscaping activities and thus not subject to Arizona's transaction privilege tax under the prime contracting classification.
  - The taxpayer used a tractor with a mastication attachment to masticate juniper and pinyon shrubs to clear grasslands.
    - The taxpayer did not remove anything from the site or uproot the shrubs.
    - Only the "above ground" parts of the shrubs were cut.
  - A.R.S. § 42-5075(I) says "the gross proceeds of sales of gross income derived from a contract for lawn maintenance services are not subject to tax under this section if the contract does not include landscaping activities."
  - The Department found that the taxpayer's activities did not constitute landscaping activities subject to tax because the taxpayer masticated only the tops of the shrubs and did not uproot the shrubs or remove the stumps.

Transaction Privilege Tax Ruling TPR16-1 Sets Out DOR's Nexus Rules for TPT

- Ruling: The substantial nexus requirement for Arizona TPT purposes is generally satisfied if any person or business resides in Arizona; maintains an inventory warehouse or place of business in Arizona; or maintains an employee, independent contractor or any other business representative or agent in Arizona.
- Ruling: For all other situations, a case-by-case determination must be made considering whether the business activities in Arizona are significantly associated with the business's ability to establish and maintain a business market in Arizona.
  - In answering that question, Arizona considers the following:
    1. The type of activities performed in Arizona by the business. The following activities may establish nexus:
       - A business employee present in Arizona for more than 2 days per year or an independent contractor or other non-employee business representative in Arizona for more than 2 days per year to promote the business's interests;
       - An office or other place of business, internet kiosk, or locally listed telephone number in Arizona;
       - Owned or leased real or personal property in Arizona;
       - Any inventory maintained in Arizona;
       - Merchandise/goods delivered into Arizona using vehicles the business owns or leases; or
       - Other activities performed in Arizona that enable the business to maintain a market in Arizona.

Transaction Privilege Tax Ruling TPR16-1 (cont.)

2. The degree of activity performed by a business that is sufficient to establish nexus depends on the following factors:
   - The function or purpose of the activity;
   - The frequency and duration of the activity; and
   - The activity's connection with or impact on the business's in-state market.

– An out-of-state business that sells merchandise to customers in Arizona may not be subject to tax if all of the following are true:
  - None of the nexus factors from No. 1 applies to the business;
  - The business makes the sale from an out-of-state location; and
  - The business delivers the merchandise to the customer by U.S. mail or common carrier only. (This is limited to agreements that include FOB shipping point provisions.)

Income Tax Legislation

Corporate Status Change Has No Arizona Income Tax Effect: H.B. 2438, Ch. 127 (2017)

- Notwithstanding any provision of the internal revenue code or any federal rule or regulation adopted under it, a change in the organizational structure of a corporation, including an S corporation, limited liability company, partnership or any other entity, into another organizational structure is not a taxable event for the purposes of Arizona income taxes if there is no change among the owners, their ownership interests, or the assets of the organization.

Spay & Neuter: H.B. 2523, Ch. 172 (2017)
New Check Off Box on Income Tax Returns

- The Department of Revenue is required to provide a space on the individual income tax return form where a taxpayer may designate an amount of the taxpayer's refund as a voluntary contribution to the Spaying and Neutering of Animals Fund.
- Also modifies the membership of the Companion Animal Spay and Neuter Committee and provides for retention of current members.
- Retroactive to tax years beginning January 1, 2017.

Income Tax Cases

ADOR v. Bosch

1 CA-TX 16-0015 (June 13, 2017)

Lesson to be learned: file Arizona income tax returns if you file federal income tax returns and appear for administrative hearings after you challenge a proposed assessment.

- Decision: Taxpayer was responsible for unpaid income taxes, interest, and penalties.
  - Taxpayer failed to file Arizona tax returns for 2000 and 2001.
  - ADOR issued proposed income tax assessments to Taxpayer based on information it had received from the IRS under I.R.C. § 6103(d)(1), which authorizes disclosure of federal income tax returns and return information to state agencies).
  - Taxpayer disagreed with assessment and requested an administrative hearing.
  - Taxpayer failed to appear at the hearing, and the hearing officer affirmed the assessments.
  - ADOR filed a tax court complaint against Taxpayer for unpaid tax, interest, and penalties.
  - ADOR moved for summary judgment, and Taxpayer opposed the motion but failed to offer any evidence showing he had filed returns in 2000 and 2001.
  - Tax court granted ADOR's Motion for Summary Judgment.
  - Taxpayer appealed, but the Court of Appeals affirmed the tax court's decision.

Income Tax Rulings

Private Taxpayer Ruling LR16-005

- Ruling: Income generated by a non-resident taxpayer performing legal services while physically present in Arizona is taxable by Arizona even though the taxpayer is not licensed to practice law in Arizona and none of the taxpayer's clients are present in Arizona.
  - The Taxpayer was a non-resident attorney licensed to practice law in the state of Washington who serves Washington clients but lives in Arizona for several months of the year even though he is not licensed to practice law in Arizona.
  - The taxpayer sought a ruling on whether his business income earned while physically in Arizona was subject to Arizona income taxation.
  - The Department found that Arizona could levy an income tax against the taxpayer for the income her earned while in Arizona under A.R.S. § 43-104(9) and Ariz. Admin. Code R15-2C-601(D)(4)(g)(iii).
  - The taxpayer made constitutional challenges to the tax. The Department disagreed:
    - The Department also found that the taxpayer's physical presence in Arizona while providing legal services to his Washington clients was enough contact with Arizona to satisfy the due process clause.
    - The Department also found that the subjecting the taxpayer to Arizona income tax was fairly apportioned and did not discriminate against interstate commerce because Washington's business and occupation tax was a tax on gross receipts, not net income, and thus, Arizona's tax on the taxpayer's income earned while physically present in Arizona did not result in double taxation or discriminate against interstate commerce.

Arizona Court of Appeals: Case Review

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Property Tax Decisions

South Point v. ADOR & Mohave County,
241 Ariz. 11, 382 P.3d 1226 (App., November 2016)

SolarCity/Sunrun v. ADOR,
242 Ariz. 395 (App. May 2017)

Loma Mariposa v. Santa Cruz County
(Memorandum Decision)

South Point

Overrules Tax Court Judgment

- Holds that Collateral Estoppel Not Effective Where the Issue of Federal Tax Preemption Had not Been Litigated – Despite Department's Attempt to Engage in Bracker Fact Finding and Analysis
- Remands Error Correction Claims and Illegal Collection claims

Effect of Decision ($24 M at Issue in Refunds)

Case remanded to make 3 determinations:

1. **Will Arizona courts apply the 9th Circuit Court of Appeals holding in *Chehalis* to a tax case resolved in an Arizona court.**

a. If not, case proceeds to *Bracker* balancing re preemption of tax policy disfavoring taxation.

b. If applicable, does it apply to personal property, real property improvements, or both.

2. Does the *Bracker* balancing test mean that federal tax policy disfavoring taxation is preempted by local interest? Totally? Partially?

3. If the case hinges on whether Chehalis enables taxing only personal property and Bracker balancing favors preemption, what portion of the plant is personal property?

4. -- Personal property and real property improvements defined under federal law. Which federal law?

SOUTH POINT

SolarCity

242 Ariz. 395 (App. May 2017)

- Upholds Tax Court ruling that ADOR may not value thousands of rooftop units owned by Solar/City and Sunrun operating as distributive generation as "electric generation facilities."
- Reverses Tax Court ruling that county assessors may value and tax taxpayer's solar rooftop property.

ADOR'S Petition for Review at Arizona Supreme Court

I. The Equipment Must Be Valued Statutorily for Tax Purposes by Either the Department or County Assessors.

A. The Department Must Value the Equipment Under A.R.S. § 42-14151(A)(4).

B. If Not the Department, Then County Assessors Must Value the Equipment Because A.R.S. § 42-11054(C)(2) Does Not Apply to Business Personal Property. See statutory valuation formula for valuing business personal property in A.R.S. § 42-13054(A) and (B).

SOLARCITY

II. If A.R.S. § 42-11054(C)(2) Applies to the Equipment, the Statute As Applied to the Plaintiffs' Equipment Violates the Exemptions and Uniformity Clauses of the Arizona Constitution.

- Exemptions Clause: All property in Arizona is subject to taxation, except as Arizona Constitution article IX and A.R.S. §§ 42-11101 through -11133 provide.
- The Arizona Constitution does not exempt from taxation equipment devoted to commercial use except as permitted in a 1996 amendment Arizona voters passed that added Article IX, § 2(6), which "*allows the legislature to exempt from taxation* a maximum of $50,000 of the full cash value of 'personal property of a taxpayer' that is used for agricultural, trade, or business purposes." See *Circle K Stores, Inc. v. Apache County*, 199 Ariz. 402, 404, ¶ 1 (App. 2001).

SOLARCITY

- Uniformity Clause: "All taxes shall be uniform upon the same class of property within the territorial limits of the authority levying the tax."
- While the Legislature can create different classifications of property, it cannot create different tax rates "for property with similar physical attributes and productiveness, used in the same way and for the same purpose by owners in the same industry."
- ADOR contends that Taxpayers compete directly with local utilities and other traditional solar generators using identical solar equipment to provide electricity to same electric customers.

SolarCity's Response to Petition for Review due on September 5.

Loma Mariposa Santa Cruz County
(Memorandum Decision)

Taxpayer submitted error correction claim to County.

County misaddressed denial letter so Taxpayer never received it.

- Held, provisions of error correction are strictly construed and failure to deliver denial to taxpayer within 60 days constituted County's acceptance of error.
- Held, taxpayer's petitions for error correction that argued that County had accepted error correction because of its failure to deliver denial did not constitute a waiver of the County's default.

Non-Property Tax Decisions

Arizona Elec. Power Coop., Inc. v. Arizona Dep't of Revenue, 242 Ariz. 85 (App. March 2017)

BSI Holdings v. Arizona Dep't of Transportation, 2017 WL 2980136 (App. July 2017)

AEPCO

Taxpayer refund claim for use tax payments for coal & natural gas purchased for electric generation

Held:

1. purchases of coal and natural gas fall do not fall“outside the scope of the Arizona use tax as nontaxable purchases for resale.”

AEPCO

- 2. coal and natural gas in the form of energy are not "[t]angible personal property that directly enters into and becomes an ingredient or component part of any manufactured, fabricated or processed article, substance or commodity for sale in the regular course of business."

BSI Holdings

Court of Appeals overturns Tax Court:

- Holds that using plain meaning of the statute the number of days an aircraft is in the state includes all or part of any day.
- Reiterates that ambiguity in a statute is only construed against taxation when all other tools of construction fail to resolve the ambiguity.

Notable Cases Pending at Court of Appeals

Wilbur-Ellis Co. v. ADOR

Phoenix et al. v. Orbitz et al.

Wilbur-Ellis Co. v. ADOR (pending at Court of Appeals)

Taxpayer claims

- tax is improper because sale of fertilizer is exempt since [t]he tax imposed on the retail classification does not apply to the gross proceeds of sales or gross income from . . . sales of propagative material to persons who use those items to commercially produce agricultural, horticultural, viticultural or floricultural crops in this state. See A.R.S. Sec. 42-5061(A)(33).

Wilbur-Ellis

- [g]ross receipts from selling tangible personal property to be resold by the purchaser in the ordinary course of business are not subject to tax under the retail classification, and the essential nutrients in its fertilizers are absorbed by and then resold as part of the plants or plant products that its customers grew. (See Arizona Administrative Code R15-5-101(A))

Wilbur-Ellis

ADOR counters:

- common dictionary meaning of “propogate” is “to cause or increase by sexual or asexual reproduction” and fertilizers do not fall within that class.
- Fertilizer is consumed by plants and is not resold when plants are sold.

Phoenix et al. v. Orbitz et al.
(Pending Court of Appeals)

Phoenix et al. includes:

- City of Phoenix
- City of Apache Junction
- City of Chandler
- City of Flagstaff
- City of Glendale
- City of Mesa
- City of Nogales
- City of Prescott
- City of Scottsdale
- City of Tempe
- City of Tucson

ORBITZ

Orbitz et al includes:

- Orbitz Worldwide Inc.
- Ortitz LLC
- Trip Network Inc. (dba Cheaptickets.com)
- Internetwork Publishing Corp. (dba Lodging.com)
- Expedia Inc.
- Priceline.com Inc.
- Travelweb LLC
- Travelocity.com LP
- Hotels.com LP
- Hotwire.com

ORBITZ

- Cities' business activity tax assessment from 2000-2009 overturned by administrative hearing officer who held that Defendants were neither hotel operators nor brokers
- Model City Tax Code relates to taxation of hotel operations.
- Tax Court holds:
- Defendants not hotels: "A hotel guest in need of clean towels would never call one of the [online travel companies]."

ORBITZ

Tax Court : Defendants' activities are taxable as "brokers." (Any person … who acts for another for consideration in the conduct of a business activity … and who received for his principal all or part of the gross activity from the taxable activity.)

- Rejects online travel companies' claims that a broker must conduct every aspect of the taxable activity, which is soliciting business and receiving customer payments.
- Holds: "Consumers purchase of the right to occupy the hotel room occurs in Arizona and nowhere else."